

## EXPERT VIEW

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# THE CASE AGAINST HIGHER FDI IN THE DEFENCE SECTOR

There was some clamour in the news that Airbus wanted the foreign direct investment (FDI) to be increased to more than 49% if India wanted to get “OEMs (original equipment manufacturers) of quality”. India needs them “a lot”. And they would be able to invest in the domestic defence sector only if they get contracts as it takes “two to tango”.

There is already a provision in the new FDI policy that permits more than 49% investment, even as high as 100%, on a case-to-case basis with the approval of the Foreign Investment Promotion Board (FIPB). Though not stated in as many words, higher FDI would be permitted only when the investment is likely to result in access to modern and ‘state-of-the-art’ technology in the country. This carefully considered clause also conveys that in national interest, government will bend backwards and make exceptions. It is for FOEMs (foreign OEMs) like Airbus to accept the challenge and provide niche cutting-edge technologies in India to earn 100% FDI.

Any further increase in FDI limit in a strategic industry like defence may not be in the long-term national interest. It surely will be a disaster for the country’s attempt to build self-reliance. Increasing FDI from 26% to 49% was really unexpected and one reason as to why Indian defence industry did not whole-heartedly welcome the increase was the fear that soon FOEMs will ask for more, and it is happening now.

India is too big a market to be ignored. Global companies that are serious about maintaining leadership position in defence will have to tap into the Indian market, for ignoring India will imperil their leadership position. If they do ignore the Indian market, companies with global position of no. 2 or no. 3 will come in, play by the rules, reinvest their profits in research and development and occupy the leadership position while dislodging the incumbent. We should therefore not be fearful that we will lose out Foreign OEMs if we don’t listen to them. That is unlikely to happen.

Supporting these too-big-to-fail companies in India is not a good idea, as it was not a good idea even in North America and Europe. They first employ people and then threaten that if contracts are not given then jobs will go. No, even from a jobs point-of-view, it is better to have anti-fragile businesses doing work for Indian defence which are lean and mean and can sustain the downturns without handholding from Indian government. So it is better that we don't "tango" with foreign OEMs especially on their absurd terms.

## COLUMN

More importantly, there are some areas in defence in which India is rapidly building capability. Companies now have cutting edge technologies and have competed with the world's best and won orders. Some are in the process of building new capabilities and technologies. Allowing higher FDI than 49% will kill Indian R&D especially as the foreign OEMs will target such budding capabilities. Indian industry needs support at this crucial juncture and keeping FDI below controlling limits would be one of the ways to support it.

The ministry should encourage development of sub-systems and equipment by Indian firms within the shortest possible time and make the procedure for procurement easier. In cases where they find that Indian companies have what the Armed forces need, the procurement process should happen within a span of six months, including request for proposal (RFP), trial, and Commercial Negotiations committee. The recent announcement of Indigenously Designed, Developed and Manufactured (IDDM) clause and some very significant changes in 'Make' procedure in the forthcoming Defence Procurement Procedure 2016 are expected to unleash the talent of committed Indian R&D firms into the defence space. Even companies that have been doing outsourcing work for defence will find it worthwhile to start developing products for the Indian market where the margins will be healthier and purchase process much improved. Already companies in various segments are moving very fast to take advantage of this lucrative defence vertical.

Foreign OEMs, with total support of their government and sometimes large Indian industrial houses, have very formidable clout. They would always make every effort to further their cause. They will ask for more and more, as it is in their interest to do it. But their demands have to be weighed against the larger national interests. Higher FDI in defence would reduce Indian partners of FOEMs to passive spectators and destroy the indigenous Indian companies. Thus noises for higher FDI have to be ignored and earnest pleas of the Indian defence industry for a conducive growth environment be heard, acted on and supported.

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